

annual **2K** report

CORPORATE PROFILE

Sheer Energy Inc. is a publicly traded oil and gas exploration and production company. Seventy-Eight percent of the Company's revenues are generated from gas production with in excess of one-half of all gas revenue being derived from an interest in the South Edson Gas Unit.

Subsequent to the fiscal year end, the Company announced that its wholly owned subsidiary, Sheer Energy (Cyprus) Limited, had reached an agreement on a Service Contract for the development of the Masjed-I-Suleyman oil field in Iran.

FINANCIAL SUMMARY

Year ended December 31	2000	1999 (restated)
Total Revenue (net of Royalties)	\$ 788,706	\$ 467,866
Cash Flow from Operations	\$ 353,049	\$ 99,147
Cash Flow from Operations per Share (Basic and Fully Diluted)	\$ 0.07	\$ 0.02
Earnings (loss)	\$ 166,112	\$ (24,664)
Earnings (loss)/share (fully diluted)	\$ 0.03	\$ (0.01)
Capital Expenditures	\$ 628,839	\$ 190,282
Total Assets	\$ 1,716,781	\$ 1,295,560
Common Shares O/S (Dec. 31)	4,837,863	4,837,863

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ANNUAL MEETING

The Annual General Meeting of the Shareholders of Sheer Energy Inc. is to be held at 3:00 p.m., Wednesday June 27, 2001 in "Salon C" of the Delta Bow Valley Hotel, 209 - 4th Avenue S.E., Calgary, Alberta.



president's message

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The 2000 fiscal year and the first few months of 2001 have seen many positive developments for your Company. Among the highlights are record year end financial results, the purchase of working and royalty interests in the Harmattan East Unit and the announcement in March 2001 that the Company's Cyprus subsidiary had reached agreement with the National Iranian Oil Company for a Service Contract for the development of the Masjed-I-Suleyman oilfield in Southern Iran.

While production for the year declined to approximately 53 barrels of oil equivalent from 69 BOE/D in the preceding fiscal year, record natural gas prices have generated record results for your Company. In excess of 78% of the Company's production is natural gas (based on 10 Mcf = 1 barrel of oil equivalent) and record gas prices have carried over into the first quarter of fiscal 2001. Many industry observers expect natural gas prices to remain at relatively high levels for the next few years until additional supplies can be brought on stream. Fiscal 2000 production declined due to property dispositions and normal production declines. Production volumes in the current fiscal year should improve due to the acquisition of the Harmattan East Unit No. 1 interest effective September 1, 2000.

Your management and Board of Directors are very pleased with the record profits and cash flow generated during the year. Earnings before taxes in fiscal 2000 were \$313,091 compared to a loss of \$22,210 in the preceding year. After tax 2000 earnings were \$166,112 (\$0.03/share) compared to a loss of \$24,664 (\$0.01/share) in the preceding year. Cash flow from operations per share in fiscal 2000 was \$353,049 (\$0.07/share) compared to \$99,147 (\$0.02/share) in the preceding fiscal year, a 356% increase.

Notwithstanding the foregoing, the most important and potentially rewarding development has been the March 13, 2001 announcement that Sheer Energy (Cyprus) Limited (49%), a wholly owned subsidiary, and its partner Naftgaran Engineering Services Company of Tehran (51%) reached agreement with the National Iranian Oil Company ("N.I.O.C.") on the terms of a "Buy-Back" agreement for the development of the Masjed-I-Suleyman (MIS) oil field in Iran. This Service Contract has been agreed as to terms and conditions subject to all necessary Iranian Government approvals, which are expected prior to the middle of June. Project operator is Sheer Energy (Cyprus) Limited.

The terms of the agreement call for the investment of approximately \$88 million U.S. Dollars over a period of four years, commencing immediately, to perform a detailed reservoir simulation study, recomplete four to six wells, drill two new vertical wells and eight horizontal wells, and construct processing and water re-injection facilities to handle the targeted production level of an incremental 20,000 barrels of oil per day. Your management is currently seeking financing for its share of the initial

2 stage of the project which is estimated to require approximately \$2 million U.S. Dollars. We are pursuing equity investment both in Canada and overseas and have met with a number of interested parties to date. We expect to be in a position to report on this further on or before our Annual General Meeting scheduled for June 27th.

Repayment of project costs and a return on investment will be made from crude oil sales over the ensuing three years from project completion. Compensation for the investment will increase or decrease for production above or below the target over the payback period.

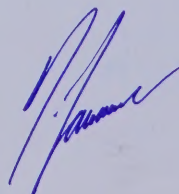
The MIS field is the first oil pool discovered in the Middle East and was initially drilled in 1908. The pool is one of several large oil fields producing from fractured carbonate rocks of the Asmari formation. The MIS field is approximately 30 km. long and 7 km. wide. Company estimates place the original oil in place at over 6 billion barrels, of which approximately 1.2 billion barrels have been produced to date. Average depth to the producing horizon is approximately 1,000 meters, with current net oil pay thickness ranging from 60 to 90 meters. The oil gravity is 40 degrees API. Current production from the pool, operated by N.I.O.C., is approximately 4,500 barrels of oil per day. N.I.O.C.'s existing production does not form part of the Service Contract.

This is an exciting opportunity to apply modern practices and technologies to achieve enhanced recoveries from a very substantial reservoir. Success at MIS may well open up additional opportunities to the Company within the project area. Success will also have significant implications for a number of other similar reservoirs in Iran.

We sincerely appreciate the patience, support and confidence of our shareholders and look forward to reporting further on these exciting developments as the year progresses.

Shareholders are reminded of the Company's Annual General Meeting scheduled for 3:00 p.m. on Wednesday June 27, 2001 at the Delta Bow Valley Hotel in Calgary.

On behalf of the Board,



April 25, 2001
Calgary, Alberta

T.D. Lawrence
President

operations review

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An evaluation of the remaining recoverable reserves and the net present value for six of the Company's properties at December 31, 2000, was recently completed by Fekete Associates Inc. An independent evaluation of the properties acquired from Krystal Energy Limited was also recently received from Matsalla Consulting (1981) Ltd.

The Matsalla report, dated at January 1, 2001, evaluates the proved producing reserves assigned to approximately 250 gas and oil wells operated by Signalta Resources Limited in which Sheer has small working interests.

The Company's net average daily production, expressed in barrels of oil equivalent per day (boe/d), declined to 53 boe/d during the fiscal year due to the disposition of the Sousa property in February 2000, the shutting in of one well at Edson due to high water cuts and normal well productivity decline. Incremental production due to the acquisition of the Harmattan property effective September 1, 2000, will likely be reflected more significantly during the first quarter 2001. The six properties evaluated by Fekete Associates produced approximately 237 Mcf/day and 9 barrels per day of crude oil and natural gas liquids net to the Company during the fiscal year, while the Krystal properties produced approximately 177 Mcf/day of natural gas and 2.5 barrels per day of crude oil and natural gas liquids.

Fekete Associates Inc. has assigned a 12% net discounted present value of \$1,942,200 to the proven plus probable reserves (probable risked at 50%) at December 31, 2000 versus a value of \$1,178,900 at December 31, 1999.

The increase in value is mostly due to the Harmattan acquisition of September 2000 and improved petroleum and natural gas prices in the latter part of the year.

Remaining recoverable reserves net to Sheer after royalties amount to 734,000 Mcf of natural gas and 46,600 barrels of oil and natural gas liquids.

The appraisal by Matsalla Consulting indicates that the remaining recoverable reserves, net after royalties, for the Krystal properties are in the order of 412,000 Mcf of natural gas and 6,700 barrels of oil and natural gas liquids, having an estimated net present value of approximately \$820,000 at a 12% discount rate.

The total remaining recoverable reserves from all the Company's properties would therefore be approximately 1,146,000 Mcf of natural gas and 53,300 barrels of oil and natural gas liquids, with a combined net present value at a 12% discount of approximately \$ 2,762,000.

The following table summarizes the net present value and the remaining recoverable reserves, net after royalties, of all the combined Canadian properties owned by Sheer.

CALCULATED NET PRESENT VALUE

@ 0%	\$ 4,642,300
@10%	\$ 2,947,930
@12%	\$ 2,762,200
@15%	\$ 2,502,654
@18%	\$ 2,300,687

REMAINING RESERVES

GAS (Mcf)	1,145,823
COND (bbls)	16,149
OIL (bbls)	30,156
NGL (bbls)	7,060

4 Following is a brief description of the units evaluated by Fekete Associates Inc.

SOUTH EDSON GAS UNIT NO. 1

Sheer has a 8.9668% working interest in the South Edson gas Unit No.1 located west of Edmonton. The Unit covers 45,120 gross acres of land and produces natural gas from the Elkton-Shunda formations at a rate of approximately 2,280 Mcf/day gross. Three wells are currently on production and five wells are shut-in or suspended. Proved producing reserves were assigned to three wells and proved non-producing reserves were assigned for the re-activation of the 10-33-49-16 W5M well. This well had been shut-in due to water loading, but it is estimated that the installation of a plunger lift system would remedy the problem. Probable additional reserves were assigned to a proposed drilling location at 11-26-50-17 W5M.

Proved producing reserves, net to Sheer, amount to 395,000 Mcf of natural gas and 8,200 barrels of natural gas liquids. Net proved non-producing reserves are 59,000 Mcf of natural gas and 1,200 barrels of natural gas liquids, while net probable additional reserves are 223,000 Mcf of natural gas and 4,800 barrels of natural gas liquids.

The 12% discounted cash flow value assigned to proved producing and non-producing reserves is \$1,063,300 while the probable, unrisks, would add another \$303,300 to the value of the property.

HARMATTAN EAST UNIT NO. 1

The Company holds a 1.014525% working interest in oil production and a 0.13331% working interest in natural gas production from the Harmattan East No. 1 Petroleum Unit and a 0.13331% interest in the natural gas production from the Harmattan East Unit No. 1 Natural Gas Unit.

The Petroleum Unit currently consists of 27 producing wells, 11 water injectors and one CO₂ injector. The Natural Gas Unit has 22 producing wells and three storage wells. Remaining recoverable reserves, net to Sheer after royalties, amount to 40,000 Mcf of natural gas and 15,400 barrels of oil and natural gas liquids. The 12% discounted cash flow assigned to the proved producing reserves is \$367,900.

The interest in these units was purchased as of September 1, 2000.

PINE CREEK

Sheer has a 5.7612% working interest in the Pine Creek Second White Specks "A" Pool Unit located west of Edmonton. Two wells are currently on production. The 12% discounted cash flow value for the proved producing reserves is calculated at \$152,700 net to Sheer's interest.

MINOR PROPERTIES

Sheer has minor working interests in three other oil units which are:

Cynthia Cardium Unit No. 4, Snipe Lake Beaverhill Lake Unit No.1 and Wainright Unit No. 6. The Company's working interest in these three units ranges from 0.076% (Snipe Lake and Wainright) to 0.32% (Cynthia).

Combined 12% discounted cash flow value for proved producing reserves, net to Sheer, is approximately \$55,000.

management's discussion & analysis

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FINANCIAL RESULTS

The 1999 comparative financial statements have been restated to correct an error by a joint venture operator in calculating the revenue allocation from an oil and gas property. The 1999 revenue has been decreased by \$80,153 with a corresponding increase to accounts payable. The current tax expense in 1999 and income tax payable were decreased by \$17,497. The resulting decrease to retained earnings was \$62,656.

PRODUCTION VOLUMES AND REVENUES

Production volumes are based on the daily production which resulted in revenues to the account of Sheer Energy Inc. The total net production to the account of the Company in 2000 was 19,360 BOE (based on the conversion of 10 Mcf equalling one barrel of liquid). Total net production for the 1999 fiscal year was 25,222 BOE.

12 months ended December 31,	2000		1999 (restated)	
	\$	\$/BOE	\$	\$/BOE
Oil & Gas Revenue	1,004,073	51.86	594,989	23.59
Royalties net of ARTC	(219,372)	(11.33)	(127,367)	(5.05)
Interest	4,005	0.21	244	0.01
Total Net Revenue	788,706	40.74	467,866	18.55
Amortization	174,837	9.03	143,078	5.67
Operating Costs	128,841	6.66	172,157	6.82
General & Administration	145,053	7.49	139,661	5.54
Interest	20,884	1.08	26,180	1.04
Income Taxes	146,979	7.59	2,454	0.10
Future Site Restoration	6,000	0.31	9,000	0.36
Net Earnings (Loss)	166,112	8.58	(24,664)	(0.98)

Revenue per barrel of oil equivalent was up 220% from the preceding year due to higher product prices.

Royalties, net of ARTC, more than doubled from \$5.05/BOE in 1999 to \$11.33/BOE in fiscal 2000. This was a function of higher product prices and a lower rate for ARTC.

Amortization per BOE increased from \$5.67 to \$9.03 as a result of the Harmattan East property acquisition.

Operating Costs decreased slightly from \$6.82 to \$6.66/BOE but actual costs were significantly lower due to lower production volumes.

In absolute terms, general and administrative expenses increased only marginally but on a BOE basis increased to \$7.49 from \$5.54 due to lower production rates in 2000.

Interest expense decreased due to lower levels of debt throughout most of the year although on a BOE basis increased slightly due to lower production rates.

Income taxes increased substantially from \$0.10/BOE in 1999 to \$7.59/BOE in 2000 due to significantly improved profitability.

Net earnings improved to \$8.58/BOE from a loss of \$0.98/BOE in 1999 due again to significantly improved profitability resulting from increased product prices.

MANAGEMENT'S REPORT

To the Shareholders of
Sheer Energy Inc.:

Management is responsible for the preparation of the Financial Statements in accordance with generally accepted accounting principles in Canada. The financial and operating information presented elsewhere in this annual report is consistent with that shown in the financial statements.

Management maintains systems of internal controls to provide reasonable assurance that assets are safeguarded and that relevant and reliable financial information is produced in a timely manner.

Hudson & Company, an independent firm of Chartered Accountants, has been engaged to examine the financial statements. Their report is presented with the financial statements. The Audit Committee of the Board of Directors has reviewed the financial statements with management and the external auditors. The Board of Directors has approved the financial statements on the recommendation of the Audit Committee.



Terrance D. Lawrence
President



Charles S. Cook
Director

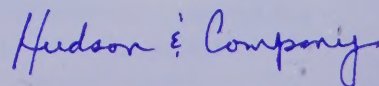
AUDITORS' REPORT

To the Shareholders of
Sheer Energy Inc.:

We have audited the consolidated balance sheets of Sheer Energy Inc. as at December 31, 2000 and 1999 and the consolidated statements of earnings, retained earnings (deficit) and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2000 and 1999 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.



Calgary, Alberta HUDSON & COMPANY LLP
April 6, 2001 Chartered Accountants

CONSOLIDATED BALANCE SHEETS

AS AT DECEMBER 31,	2000	1999 (restated)
ASSETS		
CURRENT		
Cash	\$ 6,205	\$ —
Accounts receivable	296,609	106,057
Prepaid expenses	19,137	22,474
	321,951	128,531
CAPITAL ASSETS (Note 2)	1,394,830	1,167,029
	<u>\$ 1,716,781</u>	<u>\$ 1,295,560</u>
LIABILITIES		
CURRENT		
Accounts payable	\$ 106,756	\$ 115,917
Income taxes payable	64,816	13,700
Current portion of bank credit facility	286,627	150,700
	458,199	280,317
BANK CREDIT FACILITY (Note 4)	303,741	238,614
FUTURE INCOME TAXES	215,865	209,765
FUTURE SITE RESTORATION COSTS	37,273	31,273
	<u>1,015,078</u>	<u>759,969</u>
SHAREHOLDERS' EQUITY		
SHARE CAPITAL (Note 5)	833,711	833,711
RETAINED EARNINGS (DEFICIT)	(132,008)	(298,120)
	<u>701,703</u>	<u>535,591</u>
	<u>\$ 1,716,781</u>	<u>\$ 1,295,560</u>

APPROVED ON BEHALF OF THE BOARD:



Director



Director

8 CONSOLIDATED STATEMENTS OF EARNINGS

YEARS ENDED DECEMBER 31,	2000	1999 (restated)
REVENUES		
Petroleum and natural gas sales	\$ 1,004,073	\$ 594,989
Royalties, net of Alberta Royalty Tax Credit	(219,372)	(127,367)
Interest	4,005	244
	<u>788,706</u>	<u>467,866</u>
EXPENSES		
Amortization and depletion	174,837	143,078
General and administration (Note 3)	145,053	139,661
Operating costs	128,841	172,157
Interest	20,884	26,180
Provision for site restoration	6,000	9,000
	<u>475,615</u>	<u>490,076</u>
Earnings (loss) before income taxes	<u>313,091</u>	<u>(22,210)</u>
INCOME TAXES (Note 7)		
Current	140,879	25,510
Future (benefit)	6,100	(23,056)
	<u>146,979</u>	<u>2,454</u>
NET EARNINGS (LOSS)	<u>\$ 166,112</u>	<u>\$ (24,664)</u>
Earnings (loss) per share (Note 6)		
– Basic and fully diluted	\$ 0.03	\$ (0.01)

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

YEARS ENDED DECEMBER 31	2000	1999 (restated)
RETAINED EARNINGS (DEFICIT),		
beginning of year as previously stated	\$ (235,464)	\$ (273,456)
Correction of an error (Note 9)	(62,656)	–
BALANCE, beginning of year as restated	<u>(298,120)</u>	<u>(273,456)</u>
Net earnings (loss)	166,112	(24,664)
BALANCE, end of year	<u>\$ (132,008)</u>	<u>\$ (298,120)</u>

CONSOLIDATED STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31,	2000	1999 (restated)
CASH FLOWS FROM OPERATING ACTIVITIES		
Net earnings (loss)	\$ 166,112	\$ (24,664)
Items not affecting cash	(
Amortization and depletion	174,837	143,078
Future income taxes (recovery)	6,100	(23,056)
Site restoration	6,000	3,789
Cash flows from operations	353,049	99,147
Net change in non-cash working capital balances (Note 8)	(145,260)	34,670
	207,789	133,817
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of capital assets	(628,839)	(190,282)
Proceeds from disposal of capital assets	226,200	—
Cash flows (used in) investing activities	(402,639)	(190,282)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from bank credit facility	455,625	—
Repayment of bank credit facility	(254,570)	(174,186)
Issuance of share capital, net of issue costs	—	230,651
Cash flows from financing activities	201,055	56,465
INCREASE IN CASH	6,205	—
CASH, beginning of year	—	—
CASH, end of year	\$ 6,205	\$ —
Cash flows from operations per share (Note 6)		
— Basic and fully diluted	\$ 0.07	\$ 0.02

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2000 AND 1999

GENERAL

Sheer Energy Inc. was formed at the close of business on December 31, 1998 pursuant to an amalgamation agreement between Sheer Energy Inc. and its wholly owned subsidiary, Krystal Energy Limited.

1. SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation

The consolidated financial statements include the accounts of Sheer Energy Inc. and its wholly owned subsidiary Sheer Energy (Cyprus) Limited. The subsidiary was incorporated as a limited liability company in the Republic of Cyprus on July 27, 2000. Significant intercompany accounts and transactions have been eliminated.

Cash and Equivalents

Cash and equivalents consist of cash in banks. Cash and equivalents included in the cash flows statement are comprised entirely of the balance held in foreign banks.

Capital Assets

The Company follows the full cost method of accounting for oil and gas operations, whereby all costs of exploring for and developing oil and gas properties and related reserves are capitalized. Such costs include land acquisition costs, cost of drilling both productive and non-productive wells, and geological and geophysical expenses and related overhead.

Capitalized costs, excluding costs relating to unproven properties, are depleted using the unit-of-production method based on estimated proven reserves of oil and gas before royalties as determined by independent petroleum engineers. For purposes of the depletion calculation, natural gas reserves and production are converted to equivalent volumes of crude oil based on relative sales value.

The Company applies a "ceiling test" to capitalized costs to ensure that the net costs capitalized do not exceed the estimated future net revenues from the production of its proven reserves, plus the cost of undeveloped lands, less impairment. Future net revenues are calculated at year end prices and include an allowance for estimated future general and administrative expenses, interest expense, income taxes, and capital expenditures.

Gains or losses on the disposition of oil and gas properties are not ordinarily recognized except under circumstances which result in a change in the depletion rate of 20% or more.

Amortization of furniture and office equipment is provided using the declining balance method at an annual rate of 20%.

Interest In Joint Ventures

Substantially all of the Company's oil and gas exploration and development activities are conducted jointly with others and, accordingly, the financial statements reflect only the Company's proportionate interest in such activities.

Translation of Foreign Currencies

The accounts of the foreign subsidiary were translated to Canadian dollars using the current-rate method. Under this method, assets and liabilities are translated at the exchange rate in effect at the year end and revenues and expenses at the average rate for the year. Exchange gains or losses on translation were expensed in the current year.

Future Site Restoration and Abandonment Costs

Site restoration and abandonment costs are provided for over the life of the estimated proven reserves on a unit-of-production basis. Costs are estimated each year by management in consultation with the Company's engineers based on current regulations, costs, technology and industry standards. The period charge is expensed and actual site restoration and abandonment expenditures are charged to the accumulated provision account as incurred.

Income Taxes

The Company follows the asset and liability method for accounting for income taxes. Under the asset and liability method, the change in the future tax asset and liability is to be included in income. Future tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled.

The balance of future income taxes at December 31, 2000 consists mainly of the net book value of capital assets in excess of the undepreciated capital cost and unused resource deductions, which arise from the difference between the Company's amortization and depletion rates and those prescribed for income tax purposes, and the future site restoration costs that have been expensed for accounting purposes but are only deductible for tax purposes in the year incurred.

Measurement Uncertainty

The amounts recorded for depletion, and amortization of petroleum and natural gas properties and equipment and the provision for future site restoration and abandonment costs are based on estimates. The ceiling test is based on estimates of proved reserves, production rates, oil and gas prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be significant.

Earnings Per Share

Earnings per share amounts are calculated using the weighted average number of shares outstanding during the year. Fully diluted per share calculations reflect the exercise of options and warrants at the later of the date of issuance or the beginning of the year.

2. CAPITAL ASSETS

			2000	1999
	Cost	Accumulated Amortization	Net Book Value	
Petroleum and natural gas properties and equipment				
Producing	\$ 1,534,346	\$ 449,933	\$ 1,084,413	\$ 956,024
Non-producing	306,079	—	306,079	205,582
Office furniture and fixtures	6,532	2,194	4,338	5,423
	<u>\$ 1,846,957</u>	<u>\$ 452,127</u>	<u>\$ 1,394,830</u>	<u>\$ 1,167,029</u>

3. RELATED PARTY TRANSACTIONS**Consulting Fees**

Included in general and administrative expense are consulting fees of \$60,000 (1999 – \$60,000) paid to companies controlled by officers and directors of the Company. The fees were paid under similar terms and conditions as with third parties.

4. BANK CREDIT FACILITY

	2000	1999
Production loan #1 repayable in monthly payments of \$4,225 plus interest at prime plus 1%, due October 31, 2001.	\$ 40,150	\$ 86,625
Production loan #2 repayable in monthly payments of \$8,333 plus interest at prime plus 1%, due October 31, 2001.	91,667	182,832
Production loan #3 repayable in monthly payments of \$12,857 plus interest at prime plus 1%, due November 30, 2003.	455,625	—
Demand revolving production loan with interest at prime plus 1%.	2,926	119,857
	<u>590,368</u>	<u>389,314</u>
Less current portion	<u>286,627</u>	<u>150,700</u>
	<u>\$ 303,741</u>	<u>\$ 238,614</u>

Principal repayments due as follows:

2001	\$ 286,627
2002	151,884
2003	151,857
	<u>\$ 590,368</u>

The bank credit facility allows for \$150,000 by way of account overdraft to assist with the acquisition and development of oil and gas reserves.

Collateral lodged by the Company to support the bank loans is as follows:

- (i) a debenture and general security agreement providing fixed and floating charges over all assets;
- (ii) an assignment of all risk insurance proceeds;
- (iii) environmental indemnity

5. SHARE CAPITAL

The Company has the following authorized share capital:

Unlimited number of common voting shares

Unlimited number of first preferred non-voting shares

	Number of Shares	Amount
Issued Common shares		
Issued on incorporation	2,100,003	\$ 210,003
Issued on initial public offering, net of share issue costs of \$46,943	1,450,000	228,057
Issued to acquire petroleum and natural gas properties	550,000	165,000
Issued and outstanding December 31, 1998	4,100,003	603,060
Issued in private placement, net of legal costs of \$5,850	592,860	201,651
Exercise of share options	145,000	29,000
Issued and outstanding December 31, 1999 and 2000	4,837,863	\$ 833,711

Escrow Shares

Included in shares issued is 2,100,003 common shares which were held in escrow, of which, 699,996 shares were released from escrow in 2000 (1999 – 700,001). The Company has received permission from the Alberta Securities Commission to release the remaining shares from escrow on September 14, 2001.

Stock Options

The Company has established a Stock Option Plan for the benefit of directors, officers and key employees and consultants of the Company. Pursuant to the Stock Option Plan, options for a total of 350,000 Common Shares were granted to directors of the Company on May 1, 1997. These options may be exercised within five years of issuance at a price of \$0.20 per share.

In connection with its initial public offering, the Company granted to its agent an option to purchase up to 145,000 Common Shares at a price of \$0.20 per Common Share. This option was exercised during 1999.

6. EARNINGS AND CASH FLOW PER SHARE

Basic earnings (loss) and cash flows per share amounts have been calculated based upon the weighted average number of shares outstanding during the year of 4,837,863 (1999 – 4,383,278). Fully diluted earnings (loss) and cash flows per share amounts have been based on the weighted average number of shares outstanding during the year of 5,187,863 (1999 – 5,187,828).

7. INCOME TAXES

The income tax provision differs from the expected amount calculated by applying the Canadian combined Federal and Provincial tax rate of 43.62% (1999 – 44.60%) as follows:

	2000	1999
Expected income tax (recovery)	\$ 136,570	\$ (9,906)
Non-deductible crown charge and other payments	96,916	65,422
Federal resource allowance	(76,217)	(27,871)
Alberta Royalty Tax Credit	(3,761)	(12,204)
Other	(6,529)	(12,987)
	<u>\$ 146,979</u>	<u>\$ 2,454</u>

Effective January 1, 1999 the Company changed its method of accounting for income taxes from the deferral method to the liability method (Future Income Taxes) of allocation. The retained earnings balance was decreased by \$260,296 as a result of the cumulative effect of this change to December 31, 1998.

At December 31, 2000 the Company had the following balances available to apply against future years' taxable income:

Undepreciated capital cost	\$ 121,434
Canadian oil and gas property expense	\$ 482,834
Canadian development expense	\$ 1,212
Foreign exploration and development expenses	\$ 256,968

8. STATEMENTS OF CASH FLOWS**Net Change in Non Cash Working Capital Balances**

	2000	1999
(Increase) Decrease in accounts receivable	\$ (190,552)	\$ 70,696
(Increase) Decrease in prepaid expenses	3,337	(13,684)
Increase (Decrease) in accounts payable	(9,161)	883
Increase (Decrease) in income taxes payable	51,116	(23,225)
	<u>\$ (145,260)</u>	<u>\$ 34,670</u>

Interest and Income Taxes Paid

During the year the Company had cash flows arising from interest and income taxes paid as follows:

	2000	1999
Interest paid	\$ 15,530	\$ 26,180
Income taxes paid	\$ 87,990	\$ 36,925

9. RESTATEMENT OF 1999 FINANCIAL STATEMENTS

The 1999 financial statements have been restated to correct an error by a joint venture operator in calculating the revenue allocation from an oil and gas property. The 1999 revenue has been decreased by \$80,153 with a corresponding increase to accounts payable. The current tax expense in 1999 and income tax payable were decreased by \$17,497. The resulting decrease to retained earnings was \$62,656.

10. FINANCIAL INSTRUMENTS

Credit Risk

Credit risk arises from the possibility that the entities to which the Company sells its oil and gas production to may experience difficulty and be unable to fulfill their obligations. The Company is exposed to financial risk that arises from the credit quality of the entities to which it provides services. However, due to the credit quality of the entities to which the Company sells to, credit risk and credit risk concentration is minimized.

Interest Rate Risk

Interest rate risk arises from the possibility that the value of, or cash flows related to, a financial instrument will fluctuate as a result of changes in market interest rates. The Company is exposed to financial risk that arises from the interest rate differentials between the market interest rate and the rates used on their financial instruments.

The bank credit facility bears variable interest rates. The effective interest rate realized during the year was 7.6% (1999 – 7.6%). The average interest rate was 7.3% (1999 – 7.4%).

Interest Rate Risk

The bank indebtedness bears a variable interest rate of prime plus 1%. The effective interest rate realized during the year was 5.3% (1999 – 9.3%). The average interest rate was 7.3% (1999 – 7.4%).

Fair Values

The fair values for cash, accounts receivable and accounts payable approximates their carrying values due to the short term maturity of those instruments.

The carrying values for bank credit facility and future site restoration costs approximated the fair values.

11. SEGMENTED INFORMATION

The Company's business activities are undertaken in Canada and the Middle East. The accounting policies followed by the Canadian segment are also followed by the Middle East segment.

2000	Canada	Middle East	Total
Corporate revenue	\$ 1,004,073	\$ –	\$ 1,004,073
Corporate expense	681,405	9,577	690,982
Income from operations	\$ 322,668	\$ (9,577)	\$ 313,091
Identifiable assets	\$ 1,400,159	\$ 312,284	\$ 1,712,443
Corporate assets	4,338	–	4,338
Total assets	\$ 1,404,497	\$ 312,284	\$ 1,716,781

1999	Canada	Middle East	Total
Corporate revenue	\$ 594,989	\$ –	\$ 594,989
Corporate expense	617,199	–	617,199
Income from operations	\$ (22,210)	\$ –	\$ (22,210)
Identifiable assets	\$ 1,084,555	\$ 205,582	\$ 1,290,137
Corporate assets	5,423	–	5,423
Total assets	\$ 1,089,978	\$ 205,582	\$ 1,295,560

12. SUBSEQUENT EVENT

On March 13, 2001 the Company announced that it had reached an agreement on a service contract for the Masjed-I-Suleyman (MIS) oil field in Iran. The service contract terms and conditions are subject to all necessary government approvals which are expected to be obtained within a 90 day period. Sheer Energy (Cyprus) Limited is the operator of the project and holds a 49% interest. The terms of the agreement call for total expenditures relating to the project of \$US 88 million by Sheer Energy (Cyprus) Limited and its partner Naftgaran Engineering Services Company of Tehran (51%) over a period of four years commencing immediately. Repayment will be made from crude oil sales over three years following the project completion.

corporate information

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Dario E. Sodero
Vice President and Director
Kevin M. Maguire
Treasurer and Director
Charles S. Cook
Director
Julio Poscente
Director
William C. Ranson
Secretary

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